Supreme Court, U. S.
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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-149

PETER T. STATHES, *Appellant*

v.

THE STATE OF MARYLAND, *Appellee*

**On Appeal from the Court of Special Appeals of the State of Maryland**

## JURISDICTIONAL STATEMENT

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## JURISDICTIONAL STATEMENT

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### OPINION

The opinion below was entered on December 30, 1975, and is reported at 349 A.2d 254. The portion being appealed herein is Section 1, *Jurisdiction*. A copy of the opinion appears herein as Appendix A. The Court of Appeals of Maryland, the highest court of the State, denied certiorari on May 5, 1976; a copy of the order appears as Appendix B.

## JURISDICTION

The appeal jurisdiction of this Court is invoked to review the judgment of the highest court of the State of Maryland upholding the validity of a State statute which, as applied, is repugnant to the banking laws of the United States and the criminal sanctions thereto.

### A. Nature of the Proceeding

The nature of the proceeding is a State prosecution for fraudulent misappropriation by a Federal banking institution president brought pursuant to Article 27, Section 132, of the Annotated Code of Maryland. The validity of this State statute as applied in this case was drawn in question on the ground that it overrode Federal jurisdiction and the banking laws of the United States, and the highest State court upheld its validity.

### B. Date of Judgment Below

The judgment of the Court of Special Appeals of Maryland sought to be reviewed was entered on December 30, 1975, and the mandate issued on January 29, 1976. A timely Petition for Writ of Certiorari was filed in the Court of Appeals of Maryland, the highest court of the State, and denied on May 5, 1976.

### C. Statute Conferring Jurisdiction

The statutory provision believed to confer on this Court jurisdiction of the appeal is 28 U.S.C. § 1257(2).

### D. Cases Sustaining Jurisdiction

Cases believed to sustain the jurisdiction include:

The United States Supreme Court had jurisdiction on a writ of error to review suit in a State court where validity of State statute, providing for tax on national



bank shares, is drawn in question, as being repugnant to section 548 of Title 12, prohibiting discrimination between national bank stock and moneyed capital invested in competition therewith. *First National Bank of Gutherie Central* v. *Anderson,* Iowa 1926, 46 Sect. 135, 269 U.S. 341, 70 L.Ed. 295.

The "validity" of a State statute is sustained within the meaning of § 1257(2) when the State court holds the statute applicable to a particular set of facts as against the contention that such an application is invalid on Federal grounds. *Dahnke-Walker Milling Co.* v. *Bondurant,* 257 U.S. 282; *Bantam Books, Inc.* v. *Sullivan,* 372 U.S. 58, 61 n.3. This is true even though the statute on its face bears no Federal impediment.

### E. Statutes Involved

The validity of Article 27, § 132, Annotated Code of Maryland is involved. Its text, which may be found in Volume 3A, page 148, of the official edition of the Annotated Code of Maryland, is as follows:

> If any executor, administrator, guardian, committee, trustee, receiver or any other fiduciary shall fraudulently and wilfully appropriate to any use and purpose not in the due and lawful execution of his trust, any money or any other thing of value which may come into his hands as such executor, administrator, guardian, committee, trustee, receiver, or in any other fiduciary capacity, or secrete it with a fraudulent intent to appropriate it to such use or purpose, he shall be deemed guilty of embezzlement, and shall be punished upon conviction by imprisonment in the penitentiary for not less than one year nor more than five years.

This State statute becomes invalid when made applicable to the facts in this case—prosecution of cor-

porate manager for alleged mismanagement of liquidity funds of a Federally chartered savings and loan association—because it is then repugnant to (1) Title 12 U.S.C. 1425a, "Liquidity Requirements For Members," which may be found in Volume 3, page 2518 of the United States Code (1970), and regulations promulgated thereunder by the Federal Home Loan Bank Board, 12 C.F.R. §§ 523.10-523.14, Appendix D herein; and (2) Title 18 U.S.C. § 657 which may be found in Volume 3, page 4227, United States Code (1970). The texts of these two statutes are as follows:

§ 657. LENDING, CREDIT AND INSURANCE INSTITUTIONS

Whoever, being an officer, agent or employee of or connected in any capacity with the Reconstruction Finance Corporation, Federal Deposit Insurance Corporation, Home Owners' Loan Corporation, Farm Credit Administration, Federal Housing Administration, Federal Crop Insurance Corporation, Farmers' Home Corporation, the Secretary of Agriculture acting through the Farmers' Home Administration, or any land bank, intermediate credit bank, bank for cooperatives or any lending, mortgage, insurance, credit or savings and loan corporation or association authorized or acting under the laws of the United States or any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or any small business investment company, and whoever, being a receiver of any such institution, or agent or employee of the receiver, embezzles, abstracts, purloins or willfully misapplies any moneys, funds, credits, securities or other things of value belonging to such institution, or pledged or otherwise intrusted to its care, shall be fined not more than $5,000 or imprisoned not more than five years, or both; but if the amount or value embezzled, abstracted, purloined or misapplied does not exceed $100, he shall be fined not more than $1,000 or imprisoned not more than one year, or both.



§ 1425a. LIQUIDITY REQUIREMENTS FOR MEMBERS

No member of a Federal Home Loan Bank shall make or purchase any loan at any time when its cash and obligations of the United States are not equal to such amount as the Federal Home Loan Bank Board shall by regulations prescribe: *Provided,* That such amount shall not be less than 4 per centum or more than 8 per centum of the obligation of the member on withdrawable accounts or, in the case of any member insurance company, such other base as the Board may determine to be comparable. The Board is authorized in said regulations to prescribe from time to time different amounts, within the limitations hereinbefore specified, for different classes of member institutions, and for such purposes the Board is authorized to classify such members according to type of institution, size, location, rate of withdrawals, or such other basis or bases of differentiation as the Board may deem to be reasonably necessary or appropriate for effectuating the purposes hereof. Failure to comply with the provisions hereof shall constitutue ground for removal from membership.

## QUESTION PRESENTED BY APPEAL

Whether a State can apply its general criminal statutes in such manner as to override Congressionally-established Federal jurisdiction by prosecuting the president of a Federal banking institution for the manner in which he exercised business judgment in managing the institution's liquid assets when such management was regulated by and in compliance with the Federal banking laws and was supervised by Federal regulatory agents.

## STATEMENT OF THE CASE

The appellant, Peter T. Stathes, was tried in the Circuit Court of Montgomery County, Maryland, by jury, Honorable Ralph G. Shure presiding, on two counts of an indictment charging misappropriation by a fiduciary. The first count charged the appellant beginning on or about April 6, 1967, until on or about July 20, 1973, did unlawfully while acting in the capacity of a trustee and fiduciary, embezzle and fraudulently appropriate to a use and purpose not in the due and lawful execution of his trust for and on the behalf of the Montgomery Federal Savings and Loan Association, the sum of $50,000 in violation of Article 27, Section 132 of the Annotated Code of Maryland.

The second count was identical to the first except that the time covered was July 19, 1971, until July 20, 1973.

Prior to trial Defendant's Motion To Dismiss Indictment was filed on July 31, 1974 (Docket Item # 5) claiming that the offense charged was cognizable only under Federal law and that the State court had no jurisdiction to try the accused. The State filed an opposing answer on August 28, 1974 (Docket Item # 11). A hearing on the motion was held September 3, 1974, with ruling reserved pending filing of briefs by both parties. Briefs by both parties were filed, and the motion was overruled on December 2, 1974, the first day of trial.

At the close of the State's case the defendant moved for acquittal on the basis that Federal courts have exclusive jurisdiction and the State trial court lacked jurisdiction (T, E-7) which motion was denied (T, E-25).



The jury returned its verdict of guilty on the first count, not guilty on the second.

After the verdict the defendant again filed a written motion to dismiss on the basis that the evidence clearly showed that the State trial court lacked jurisdiction (Docket Item # 90 filed December 12, 1974). On December 13, 1974, defendant requested a hearing on his Motion To Dismiss (Docket Item # 92), but it does not appear from the record that either a hearing was held or that the motion was ever acted on. Defendant was sentenced to three years confinement with two years suspended.

Thereafter a timely appeal was taken in which the Federal jurisdictional question was vigorously urged but was rejected by the Court of Special Appeals of Maryland whose opinion appears in Appendix A.

After a successful career in private real estate financing appellant founded Montgomery Federal Savings and Loan Association in 1959 and became its president and general managing officer. Because the Association could not afford to pay him a full salary during its early years he divided his time between the Association and his other business from which he became semi-retired. This arrangement was maintained with the full knowledge and consent of the Association's directors and with full knowledge and under supervision of the Federal Home Loan Bank Board.

The Federal Home Loan Bank Board not only issues pervasive regulations covering every aspect of a savings and loan association's operations, but through its Office of Examinations and Supervision maintains direct and continuous administrative supervision. Assistant Chief Examiner John R. Amick testified

in this case that the purpose of his on-site examinations of individual associations was to determine that they are complying with the regulations and that their policies and procedures would not impair the depositors and/or shareholders. More particularly, he stated that examiners routinely examine ledger cards and reports pertaining to checking accounts and determine the association's liquidity needs and what they were maintaining as liquid assets. He testified also that it was usual practice for associations to maintain several operational checking accounts and that inactive accounts maintained by an association without operating problems would be regarded as proper convenience accounts or correspondence accounts with banks. He defined a convenience account as one opened at a bank where an association might want to obtain a line of credit in the future. He concluded that they were evaluated from his standpoint as they affected the overall earnings of the association and that it was basically a matter of prudent management policy.

Supervisory personnel of the Office of Examinations received monthly and semi-annual financial reports from Montgomery Federal and made on-site examinations every 12 to 14 months. These examinations consisted of two or three Federal examiners spending three weeks in the Association's office probing through its books and records. On one occasion these examiners also conducted an extensive on-site examination of appellant's private office and verified that there were no improper dealings. Although called as a witness for the prosecution, he did not implicate appellant in any improper acts nor did he find that the Association's funds had been used in any improper manner.



The General Counsel for the Association testified that Federal examination reports for the years covered by the indictment (1967 through 1972) in comments or critiques never questioned the checking account that was the subject of the indictment.

Regulations promulgated by the Federal Home Loan Bank Board definitively prescribe the allocation of deposits and other assets into long-term loans and liquidity funds and further regulate the manner of handling funds in each of these categories. The regulations relating to the handling of liquidity and liquid assets are reproduced herein as Appendix D.

The savings and loan business consists of soliciting deposits from the public and investing the bulk of the deposits in long-term first mortgage loans on real estate. A minimum percentage of the deposits must be maintained in liquid form to meet the demands for withdrawals, current expenses and new loan commitments.

As the managing officer it was appellant's responsibility to maintain the overall profitability of the Association—to get new accounts, hold existing depositors and invest funds profitably. Profit management requires the skill to make many intangible judgments in a constantly changing ambiguous economic environment—how many employees, what pay levels, how much advertising, how to attract new customers—judgments that are quite different from those required of the trustee of a testamentary trust estate.

Appellant was the first president of the Association and continued in that capacity until charged in the instant case. Starting with a bare $75,000 in capital the Association always paid the highest dividend per-

mitted by law and grew to a $26,000,000 asset size with $1,000,000 in reserves and surplus during the time appellant served as president.

The prosecuting witness was Joel Kline, a man whose business was purchasing and selling real estate for speculation and using as much borrowed money as possible. His testimony recounts unusual time, effort and money spent in cultivating personal relationships to maximize his borrowings, utilizing many banks, building and loan associations and other business contacts.

M & J Inc., a corporation in which he had an interest, placed several first trust loans with Montgomery Federal, all of which were conservative loans and all of which were trouble free, according to prosecution witness Yadin, a principal of M & J.

Prior to 1973 Kline was well known and well thought of in the business community. In 1966 he and two of his associates opened substantial savings accounts in Montgomery Federal. In 1967 he proposed to appellant that he would deposit an additional $50,000 in Montgomery Federal if Montgomery Federal would put an equal amount of the money kept in checking account funds in a checking account at Citizens Bank and Trust Co. This account was approved by the Montgomery Federal directors whose policy was to encourage new business and to open courtesy accounts for this purpose, and the account was opened in Montgomery Federal's name and under Montgomery Federal's control.

The opening and maintaining of this account is the alleged fraudulent misappropriation of funds charged in Count One of the indictment. It was opened as a



cash item as defined in the Liquidity Regulations, § 523.10(a) which provides: "The term 'cash' means cash on hand and unpledged demand deposits in . . . an insured bank . . ."

The account was maintained in the name of, and under the full control of, the Association. It was not pledged in any manner by the Association or the appellant nor was any authority given to anyone to use it as a compensating balance for Kline. The balance of each checking account maintained by the Association was reported monthly to the directors and to the Federal Home Loan Bank Board.

At that time Montgomery Federal maintained checking account balances totalling a minimum of $300,000 as a matter of operating policy. This amount was divided among several banks and in opening this new account the total balance was not increased but reallocated within the same total.

This was a good transaction for Montgomery Federal because it gave the Association in excess of $50,000 in new deposits on which it earned an average of two percent above dividends paid thereon.

In 1973 Kline's fortunes turned, he was declared bankrupt involuntarily and was indicted for nine counts of perjury and one count of obstruction of justice which related to an SEC investigation of his affairs. He pled guilty to the one count of obstructing justice and was given immunity from further prosecution on condition that he testify against others.

The State prosecutors ignored the reciprocal deposit of Kline and the fact that the total amount of the Association's money in checking accounts did not increase

and procured an indictment and conviction of appellant for fraudulent misappropriation arguing that since Montgomery Federal's $50,000 was placed in a non-interest bearing account its depositors lost the interest that should have been earned on this money and that this combined with hospitality and favors extended appellant by Kline constituted fraudulent misappropriation. This act of opening an additional checking account in the Association's name and under its control would not be a crime under Federal law. It would not constitute a misapplication of funds, and there was no evidence of conversion or wrongful intent to defraud the Association.

## SUBSTANTIAL FEDERAL QUESTIONS

The highest court of the State of Maryland decided this case in a way not in accord with the applicable decisions of this Court, other Federal and state courts and not in accord with its own prior decisions. By this case it is attempting to establish a distinction which, if allowed, will permit general state criminal statutes to override Congressionally-established exclusive Federal jurisdiction.

Congress has provided a pervasive regulatory scheme for national banks (12 U.S.C. § 1 et seq.) and Federal savings and loan associations (12 U.S.C. § 1421 et seq.) which are similar and parallel in every respect pertinent to the facts of this case. In particular, the criminal sanctions for malfeasance by officers and employees are virtually identical—18 U.S.C. § 656 applies to national banks, while 18 U.S.C. § 657 applies to Federally chartered savings and loan corporations. The prohibition against one who "wilfully misapplies" in both of these parallel Federal statutes certainly covers



and therefore preempts the general "fraudulent misappropriation by a fiduciary" State statute when applied to the internal affairs of a Federal savings and loan corporation.

There is a consistent line of cases holding that the Federal government has preemptive jurisdiction in matters concerning criminal prosecutions of officers and employees of banks created and regulated by acts of Congress.

Starting with *Commonwealth* v. *Ketner,* 92 Pa. 372, 37 Am.Rep. 692 (1880), the Supreme Court of Pennsylvania stated that "the national banks are the creations of another sovereignty. They were created and are now regulated by the acts of Congress . . . " State law cannot "by mere implication be extended to national banks for the reason that the affairs of such banks are exclusively under the control of congress." In this habeas corpus action the accused who had been indicted in the state court for embezzlement from a national bank was ordered to be discharged.

The Supreme Court of Michigan confirmed the holding of *Ketner* in *People* v. *Fonda,* 62 Mich. 401, 29 N.W. 26 (1886) quoting the Constitution, Article VI which provides:

> This Constitution and the laws of the United States . . . shall be the supreme laws of the land; and the judges in every state shall be bound thereby, anything in the constitution or laws of any State to the contrary notwithstanding,

the court goes on to say, "An examination of this statute (U.S. banking) must convince anyone that the offense described in this information is clearly defined and falls within the jurisdiction of the federal court

and if that jurisdiction is exclusive in the case but little remains to be said,—if it is, the conviction cannot be maintained.

" . . . Congress by law created the national banking system and provided for their internal workings and prescribed a punishment for the offenses charged against the respondent. . . . by federal law itself the jurisdiction of the state is expressly excluded."

The defendant had been tried, convicted and sentenced under state law for embezzlement while a national bank employee. The judgment was reversed and the prisoner was ordered discharged.

In 1889 a national bank officer was indicted concurrently by the State of Virginia and the United States for the same act of embezzlement and misapplying bank funds. He filed a motion in the United States Court to postpone since prosecution had already commenced in the state court for the same acts charged here. The motion was denied on the basis that " . . . the trial of officers of national banks who are charged with abstracting, embezzling or misapplying moneys, funds or credits of those banks is within the exclusive jurisdiction of the courts of the United States, and, being exclusively so, the trial cannot proceed in other courts." *U. S.* v. *Buskey,* 38 F. 99 (1889).

The court went on to observe, "It is true that the courts of two or three other states have held otherwise, but in all such decisions the phrase 'exclusive jurisdiction' is construed to mean 'concurrent jurisdiction,' and the term 'exclusive' is held to mean 'non exclusive.' I am sorry that my own mind is incapable of comprehending the logic by which plain words having plain meanings are thus metamorphosed into other words with other meanings."



In that same year, 1889, this Court in *Cross* v. *North Carolina,* 132 U.S. 131, 33 L.Ed. 287, 10 S.Ct. 47, distinguished between crimes defined and punishable at common law or by the general statutes of a state and crimes cognizable under the authority of the United States and held forgery of a note to be of the former while entering the forged note on the books of a national bank by an officer of that bank to be of the latter.

In 1893 the precise point which the Maryland court herein now holds is a "distinction" was decided in *In re Eno,* 54 F. 669, subsequently reversed on another issue, 155 U.S. 89, 15 S.Ct. 30, 39 L.Ed. 80. New York did not dispute that the United States had jurisdiction over crimes committed by a national bank officer but contended that the state also had jurisdiction because the crimes are also offenses against the people of the state. Petitioner was ordered discharged because the "conclusion seems inevitable that the offenses . . . are exclusively cognizable by the courts of the United States."

In 1903 this Court went into the subject thoroughly in the case of *Easton* v. *Iowa,* 188 U.S. 220, 47 L.Ed. 452, 23 S.Ct. 288. There the president of a national bank was tried and sentenced to the penitentiary under a state statute for accepting a deposit when he knew the bank to be insolvent This Court reversed the conviction pointing out that the Federal legislation was passed to erect a system extending through the country independent of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various as the states; Congress has provided a symmetrical and complete scheme for the banks; confusion would necessarily result from control possessed and exercised by two independent au-

thorities; officers could be in full compliance with Federal law and at the same time imprisoned under state law, consequently the Federal law cannot be overridden by the state. A number of state and Federal cases are cited and analyzed, all of which uphold exclusive Federal jurisdiction. Most of these cases involve general state criminal statutes as distinguished from special crimes applicable to bank employees only.

The instant case is analogous to *Easton* in two important respects: (1) the liquidity regulations provided by Congress pertinent herein are analogous to the insolvency provisions in *Easton;* (2) appellant herein has been convicted under state law while acting in compliance with Federal law.

The cases are admittedly old, but they established the law which has not changed. The only case since then, *Martin* v. *State,* 61 S.W. 2d 999 (1933) is to the same effect. There the assistant cashier of a Federal Reserve member bank was convicted under the general state embezzlement statute. The Court of Criminal Appeals of Texas reversed the judgment and dismissed the prosecution concluding that Congress, having power to do so, "has directly dealt with the subject of embezzlement by an officer of a member bank of the Federal Reserve System and has provided a penalty therefor, and that jurisdiction to punish any officer . . . of any member bank . . . is vested in the courts of the United States exclusive of the courts of the several states."

The Maryland Court of Special Appeals in the instant case purports to find *Easton* distinguishable and *Martin* factually parallel to *Easton.* On careful reading it appears that the appeals court has misinterpreted *Easton* and mistaken the statute under which *Martin* was prosecuted. In *Martin* the Texas appeals court referred to two state statutes in its opinion—one the general statute denouncing embezzlement and the other a special law prohibiting state bank officers and agents from embezzling, fraudulently abstracting or wilfully misapplying bank funds. Both of these state statutes are quoted on page 1001 of the opinion, and the Maryland court mistakenly states that Martin was indicted under the special law, article 544, Texas Penal Code. In the middle of column one it clearly states, "The indictment in this case was brought under and by virtue of the general statute . . . article 1534, Texas Penal Code." Consequently the holding is opposite to what the Maryland court assumed it to be, and it weighs heavily against the court's contention.



While the state statute in *Easton* was a special statute relating only to punishment of bank employees, the reasoning of the case and the numerous citations lend no support to the Maryland court's contention that it permits general state statutes to override preemptive Federal law while limiting only "special" statutes in this regard.

On June 30, 1975, the Court of Appeals of Maryland decided *First National Bank of Southern Maryland* v. *U. S. Fidelity and Guaranty Co.,* 340 A.2d 275, 275 Md. 400. There the court applied the proper law in the proper way, but it failed to apply that same law in the same way herein.

In the case herein the court is holding that there is no Federal law that is supreme, that the general criminal law of Maryland enjoys concurrent and equal footing with any Federal law limited only by the geo-

graphical boundaries of the State of Maryland. This is contra to Article VI of the Constitution.

The cases cited by the Maryland court of special appeals for the proposition that both sovereigns can prosecute under the circumstances of this case do not so hold. *U. S.* v. *Lanza,* 260 U.S. 377, 382, is a Volstead Act case under the Eighteenth Amendment which expressly confers concurrent jurisdiction. The quote that a crime under both Federal and state sovereignties can be punished by each is attributed to *U. S.* v. *Jackson,* 470 F.2d 684, a check forgery case. The *Jackson* opinion discloses that the quote originated in *Lanza,* the Eighteenth Amendment case. As was previously pointed out under *Cross* v. *North Carolina,* forgery is in the area of concurrent jurisdiction.

In the instant case the questioned offense was committed by an officer and employee of a Federal savings and loan association within the scope of his employment. The subject matter of the crime was the management of liquidity funds. Management of such funds is covered by laws and regulations established by the U. S. Congress for Federally chartered associations, and any dereliction of duty in handling such funds involving misapplication and criminal intent is by Congressional design to be prosecuted under 18 U.S.C. § 657. Under the Constitution these Congressional enactments are the supreme law of the land, and the Maryland court has erred in attempting to override them.

The question is important because there are hundreds of national banks and Federally insured savings and loan corporations in Maryland and thousands of such associations across the country located in states



which have similar laws to Maryland's. If this decision is permitted to stand, it will disrupt the goal of uniformity of Federal procedure in the regulation of Federally chartered and Federally insured savings and loan association and possibly national banks as well.

While this Court has spoken out clearly on the preemption of Federal regulation of national banks, it appears that it has not ruled on the status of Federally chartered savings and loan corporations. As this case demonstrates, it would be beneficial to the Federal regulatory scheme for this to be done, and this case would provide a suitable vehicle.

## CONCLUSION

It is submitted that the question presented by this appeal is substantial and of public importance warranting plenary consideration by this Court.

Respectfully submitted,

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July 31, 1976

# APPENDIX

## APPENDIX A

COURT OF SPECIAL APPEALS OF MARYLAND.

No. 237.

PETER T. STATHES

v.

STATE OF MARYLAND.

Dec. 30, 1975.

* * *

Argued before MENCHINE, LOWE and MELVIN, JJ.

MENCHINE, *Judge.*

On July 17, 1974 Peter T. Stathes, a former president of Montgomery Federal Savings and Loan Association, was indicted by the Grand Jury of Montgomery County on two counts of fraudulent misappropriation as a fiduciary in violation of Maryland Code Article 27, § 132. Brought to trial before a jury in the Circuit Court for Montgomery County (Shure, J., presiding) Stathes was found guilty under the first count that reads as follows:

> *"Fraudulent Misappropriation by Fiduciary*
>
> The Grand Jurors of the State of Maryland, for the body of Montgomery County, upon their oaths and affirmations, present that Peter T. Stathes, late of said County, beginning on or about April 6, 1967, until on or about July 20, 1973, at the County aforesaid, did unlawfully, while acting in the capacity of a trustee and fiduciary, embezzle and fraudulently and wilfully appropriate to a use and purpose not in the due and lawful execution of his trust for and on the behalf of The Montgomery Federal Savings and Loan Association, the sum of Fifty Thousand Dollars ($50,000.00), current money, in violation of Article 27, Section 132 of the Annotated Code of Maryland, contrary to the

form of the Act of Assembly in such case made and provided and against the peace, government and dignity of the State."

The count had been particularized as follows:

"Comes now the State of Maryland and provides the following Bill of Particulars surrounding the allegations of the Indictment filed herein:

"Count I: That beginning on or about April 27, 1976, until on or about July 20, 1973, the defendant, then in a position of trust and acting in a fiduciary relationship to the shareholders in The Montgomery Federal Savings and Loan Association, caused certain monies of said Association to be deposited in the Citizen's Bank and Trust Company of Maryland, pursuant to an agreement with Joel T. Kline. These monies were to remain in non-interest bearing accounts to act as compensating balances on loans made by the Citizen's Bank and Trust Company of Maryland to companies in which Joel T. Kline had an interest. The defendant agreed to this arrangement in return for certain favors and benefits rendered or to be rendered to the defendant by Joel T. Kline."

Stathes was sentenced conditionally to a term of three years imprisonment under the provisions of Code Article 27, § 641 A.

His appeal to this Court thus phrases the questions presented:

"1. Was the Circuit Court without jurisdiction to try appellant, an officer and director of a federally chartered savings and loan association, upon an Indictment charging embezzlement in violation of Article 27, Section 132 of the Code?

2. Did the court below err in its instructions to the jury (a) by failing to instruct on the requisite fraudulent intent needed for conviction of a violation of Article 27, Section 132, and (b) by failing to instruct properly on the necessity for corroboration of the testimony of an accomplice?

3. Did the court below err by unduly restricting the cross-examination of two of the State's witnesses in violation of the appellant's constitutional right to confront the witnesses against him?

4. Was there sufficient evidence (a) to corroborate the testimony of an accomplice that appellant opened a checking account as a compensating balance for said accomplice, or (b) to show that appellant had the specific intent necessary to sustain a conviction under the statute?"



### 1. *Jurisdiction*

Appellant contends that Montgomery Federal Savings and Loan Association as a federally chartered savings and loan association is an "instrumentality and agency of the United States, not subject to state regulation or control." From that undisputed premise, he argues that State courts are without jurisdiction to prosecute him, contending that Congress has provided a complete and pervasive scheme to regulate federal savings and loan associations under Title 12—Banks and Banking, Ch. 12—Federal Savings and Loan Associations, Section 1461 *et seq.* and has by 18 U.S.C.A. § 657 imposed criminal penalties upon officers of such associations for embezzlement.[1] Otherwise stated,

[1] We note that the provisions of Title 18 U.S.C.A. § 3231 provide:

"The district courts of the United States shall have original jurisdiction, exclusive of the courts of the States, of all offenses against the laws of the United States.

"Nothing in this title shall be held to take away or impair the jurisdiction of the courts of the several States under the laws thereof."

appellant contends that Congress has placed such criminal conduct within the exclusive jurisdiction of the federal courts.

Appellant's principal reliance is upon the cases of *Easton* v. *Iowa,* 188 U.S. 220, 23 S.Ct. 288, 47 L.Ed. 452 (1903); and two State decisions, namely: *Martin* v. *State,* 124 Tex. Cr. 246, 61 S.W.2d 999 (1933); and *State* v. *Thornton,* 171 Minn. 466, 214 N.W. 279 (1927). We find *Easton, supra,* to be readily distinguishable. In *Easton,* the Iowa statute consisted of two sections that: (a) prohibited *every* bank "when insolvent, [to] accept or receive [any] deposit," and (b) imposed criminal liability upon "any owner, officer, director, cashier, manager, member, or person knowing of such insolvency who shall knowingly receive or accept * * * any such deposits * * * ." In reversing state conviction in *Easton,* the Supreme Court said at 188 U.S. 231-32, 23 S.Ct. at 291, 47 L.Ed. at 457:

> "But we are unable to perceive that Congress intended to leave the field open for the states to attempt to promote the welfare and stability of national banks by direct legislation. If they had such power it would have to be exercised and limited by their own discretion, and confusion would necessarily result from control possessed and exercised by two independent authorities.
>
> "Nor can we concede that by such legislation of a state as was attempted in this instance, the affairs of a national bank, or the security of its creditors, would be advantageously affected. The provision of the state statute is express that it is the duty of the officers of the bank, when they know it is insolvent, to at once suspend its active operations; for it is obvious that to refuse to accept deposits would be equivalent to a cessation of business. Whether a bank is or is not actually insolvent may be, often, a question hard to answer. There may be good reason to believe that, though temporarily embarrassed, the bank's affairs may take a fortunate turn. Some of the assets that cannot at once be converted into money may be of a character to justify the expectation that, if actual and open insolvency be avoided, they may be ultimately collectible, and thus the ruin of the bank and its creditors be prevented. *McDonald* v. *Chemical Nat. Bank,* 174 U.S. 610, 43 L. Ed. 1106, 19 S.Ct. 787. But, under the state statute, no such conservative action can be followed by the officers of the bank except at the risk of the penalties of fine and imprisonment. In such a case the provisions of the Federal statute would permit the Comptroller to withhold closing the bank, and to give an opportunity to escape final insolvency. It would seem that such an exercise of discretion on the part of the Comptroller would, in many cases, be better for all concerned than the unyielding course of action prescribed by the state law. However, it is not our province to vindicate the policy of the Federal statute, but to declare that it cannot be overridden by the policy of the state."



In *Martin, supra,* as in *Easton,* the statute in question had attempted to extend the effect of a state law set up to control banking institutions so as to have application to national banks. The case therefore factually is parallel to *Easton* and similarly distinguishable.

In *Thornton, supra,* the Supreme Court of Minnesota made special note that the State indictment "appears to be drawn with painstaking care to state an offense under section 5209, Rev.St. of the United States" (214 N.W. p. 280). There is nothing in the opinion to indicate that the offense charged was in violation of any Minnesota statute. There is little wonder that, under such circumstances, the Court said (p. 279) " * * * any offense against the [Federal] statute cited is within the exclusive jurisdiction of the federal courts."

We do not interpret the decision in *Easton* as pre-empting State prosecution or compelling exclusive Federal jurisdiction in the prosecution of general criminal offenses proscribed by both Federal and State statutes. We do not regard the subject statute as constituting in any sense an attempt by the State to override the policy of a federal statute. On the contrary, we regard this State penal statute, applicable to all persons within its borders, to have no relationship to an attempt to assert control of federally chartered associations. It merely provides for the punishment of an act that is criminal under the laws of both State and Federal Governments. The right of different sovereignties to prosecute in such circumstances is well recognized. *Westfall* v. *U. S.*, 274 U.S. 256, 47 S.Ct. 629, 71 L. Ed. 1036 (1927); *U. S.* v. *Lanza*, 260 U.S. 377, 382, 43 S.Ct. 141, 142, 67 L.Ed. 314, 317 (1922); *U. S.* v. *Jackson*, 470 F.2d 684 (5th Cir., 1972). In *U. S.* v. *Jackson, supra*, the Court clearly and succinctly stated the rule we apply to the subject case when it said in 689:

> "An act denounced as a crime by both federal and state sovereignties is an offense against the peace and dignity of both, and may be punished by each."

2. *Instructions*

(a) *Alleged failure to instruct as to fraudulent intent*

Appellant contends that it was essential that the jury be sufficiently instructed as to the required specific statutory intent and argues that the charge of the court failed to do so. We do not see it that way.

It is an undisputed fact that the appellant was president of Montgomery Federal Savings and Loan Association. As such he stood in a fiduciary relationship to the corporation and thus would not be permitted under any circumstances to use the powers entrusted to him to promote his personal interests at the expense of the corporation. *Coffman* v. *Maryland Publishing Co.*, 167 Md. 275, 289, 173 A. 248, 254 (1934).



The charge of the court must be considered in the light of this circumstance. The charge of the court included, *inter alia*, the following:

> "Now, we are here dealing with criminal breach of fiduciary duty, specific violations of Article 27, Section 132 of the Annotated Code of Maryland. This section deals with crimes and punishments, and I have had a photocopy made of this section which the foreman can take into the jury room with you for your deliberation.[2] * * * He is charged with a violation of this fiduciary duty, and it is, therefore, for you to determine whether he is or is not guilty, guilty being necessary beyond any reasonable doubt, as I have previously indicated. * * *
>
> "The Defendant contends that he did not embezzle or in any way misuse the funds of the shareholders and that the deposits made in the banks in question were approved by the Board of Directors and were for legitimate business purposes only; such as, creating goodwill, solicitation of new accounts and ordinary business operations wherein checking accounts were

[2] Article 27, § 132 reads as follows:

> "§ 132. *Fraudulent misappropriation by fiduciaries.*
>
> If any executor, administrator, guardian, committee, trustee, receiver or any other fiduciary shall fraudulently and willfully appropriate to any use and purpose not in the due and lawful execution of his trust, any money or any other thing of value which may come into his hands as such executor, administrator, guardian, committee, trustee, receiver, or in any other fiduciary capacity, or secrete it with a fraudulent intent to appropriate it to such use or purpose, he shall be deemed guilty of embezzlement, and shall be punished upon conviction by imprisonment in the penitentiary for not less than one year nor more than five years."

necessary. The Defendant was acting in a fiduciary capacity as President and Director, and it is for you to determine whether or not he had, first, the ability to control; and secondly, did so control and arrange for the use of funds or compensating balances or otherwise as favors in exchange for favors from Mr. Kline and his associates. If he did use the savings and loan association funds in this manner this constitutes criminal intent and your verdict must be guilty. If you do not so find, your verdict must be not guilty.''

We note that the full text of the criminal statute had been given to the jury by the trial judge. This action caused its language to be incorporated in the charge by reference. This tended to insure that the jury was fully advised that proof of a specific fraudulent intent was an element of the State's burden. In *Andresen* v. *State,* 24 Md.App. 128, at 191-92, 331 A.2d 78, at 116 (1975), we said:

*''Elements of Fraudulent Misappropriation by a Fiduciary*

The appellant now claims that he objected to the failure of the trial court to define the elements of the crime of fraudulent misappropriation by a fiduciary, although he admits that his objection was 'inartfully worded.' That is the most artful of understatements, since the confrontation consisted only of the following:

'The Court: . . . As far as the other objections are concerned, there are certain instructions that I gave the jury that have not come from case law, necessarily, Maryland case law, but in order to apprise the jury of the requirements under the various counts, I think it is necessary to explain to them the elements of the crime that needed to be proven, and sometimes you can't find that particular element defined; therefore you've got to go elsewhere.



'Mr. Lamb: I would submit that that would be where the judge is the determiner of the law, but in Maryland the jury is the finder of facts.'

We cannot glean the remotest 'inartful' suggestion of the objection now being pressed. The judge had, moreover, read to the jury the full text of Article 27, § 132.''

We believe that the overall charge of the trial court fairly and adequately instructed the jury that the State was required to show a specific intent or special *mens rea* of fraud and wilfulness. This is all that was required. *Gordon* v. *State,* 14 Md.App. 245, 258-59, 286 A.2d 833, 842 (1972).

(b) *Failing to instruct properly on the necessity for corroboration of an accomplice*

The record shows that the appellant did not seek an instruction on the necessity for corroboration of the testimony of an accomplice. The issue is not before us. Rule 756 g.

In *Brown* v. *State,* 14 Md.App. 415, 422, 287 A.2d 62, 65 (1972) we said:

'' * * * we think that as a general guide, we may say that under Rule 756 g we will take cognizance of and correct an irremediable error of commission, but not an error of omission. Of course, the error must be plain, and material to the rights of the accused, and, even then, the exercise of our discretion to correct it should be limited to those cases in which correction is necessary to serve the ends of fundamental fairness and substantial justice.

''The omission here was one which the trial court could have, and undoubtedly would have, supplied by a supplementary instruction if appellant had requested it before the jury retired to consider its verdict.''

That rule is particularly apposite in the subject case. The sole objection to the trial court's charge relating to the testimony of an accomplice had been as follows:

> "We object on the grounds of omission from the charge to the Court omitting to give the jury our instruction or charge relating to the great care with which the jury must view the testimony of accomplices."

The trial court had included in its charge the following:

> "As you will recall, the State has presented certain alleged accomplices in connection with the use of funds claimed to be for compensating balances. One of the witnesses, Mr. Kline, has been granted immunity from prosecution in exchange for his testimony in this case. This is proper for the prosecution to do, and this is a recognized use in the means of law enforcement. This testimony, however, must be weighed carefully, along with all of the other testimony, and you give it such weight as in your judgment it is fairly entitled to receive."

The record fails to include the instruction that had been sought by the appellant. In its absence, the exception indicates merely that the appellant requested that the jury be alerted to the need for careful examination of the testimony of an accomplice. The charge as given adequately did so. We do not intimate, of course, that the uncorroborated testimony of an accomplice would serve as legally sufficient evidence to convict.

### 3. *Restrictions on Cross-Examination*

Appellant contends that cross-examination was wrongfully curtailed to the point where appellant's constitutional right to confrontation was denied.



#### (a) *The witness Kline*

Extensive cross-examination was permitted with respect to Kline's character as the following excerpts from the record will demonstrate:

> "Q. And did you from time to time offer money or things of value in connection with appointments to federal office?
>
> A. Yes, sir.
>
> Q. And did you from time to time offer money and things of value in connection with an appointment to State office?
>
> A. Yes, sir.
>
> Q. And did you from time to time in connection with appointments to State, Federal or County offices offer substantial sums of money?
>
> A. Yes, sir.
>
> Q. And did this conduct extend over a period of time?
>
> A. Yes, sir.
>
> Q. And did this extend to the law enforcement officials?
>
> A. Yes, sir.
>
> Q. And did this extend to the offices of the Executive Department of the Federal Government?
>
> A. Yes, sir.
>
> Q. And did this extend to the Banking and Insurance Department within the State of Maryland?
>
> A. Yes, sir.
>
> Q. And did you at one time discuss with persons, with people the offering of money or things of value so that you, yourself, might hold the office of Banking Commissioner of the State of Maryland?
>
> A. Yes, sir.
>
> * * * * * * * * *
>
> Q. And did you have similar discussions with other persons in the State of Maryland regarding the offer-

ing of money or things of value so that other people might get other appointments?

A. Yes, sir.

Q. And did this cover Executive offices, that is, offices of the Executive Branch of the Government of the State of Maryland?

A. Yes, sir.

Q. And that is other than the Banking Commissioner?

A. Yes, sir."

It had been elicited from Kline in his direct examination that he had pleaded guilty to conspiracy to obstruct justice in that in 1972 "[he] and others were telling the witnesses how to testify and were obstructing justice * * * ." The record also showed the following:

> "THE WITNESS: There is an agreement that was entered into between myself and the State of Maryland with a promise not to prosecute me for any criminal activity in return for my cooperation in future criminal prosecution, with the understanding that if I should perjure myself or not be candid this agreement, I believe, will become null and void and I could be prosecuted, and anything I said could be used against me."

Such was the setting when a sustained objection by the State prevented counsel for appellant from showing the specifics of Kline's conduct and from obtaining the names of the other persons allegedly involved. The State's Attorney had objected to such an inquiry because the proposed evidence was not relevant to the trial of the case; was not proper impeachment; and might have a substantial deterrent effect upon pending federal investigations.

In the course of the discussion upon impeachment of a witness by cross-examination to show bad character as evi-



denced by conduct, it is said in 3A Wigmore, *Evidence,* § 983 (Chadbourn rev. 1970) at 847:

> "(2) By the rule obtaining in most jurisdictions of the United States, the repression of possible abuses is left in the *discretion of the trial judge;* questions upon facts relevant to character may still be forbidden by him where he believes that under the circumstances it is unnecessary and undesirable."

The following quotation from *Kruszewski* v. *Holz,* 265 Md. 434, 440, 290 A.2d 534, 538 (1972), not only demonstrates that Maryland adheres to that general rule, but the language of the Court tends as well to demonstrate that the sustaining of the objection in the subject case did not constitute an abuse of discretion:

> "It is well settled law in this State that exploratory questions on cross-examination are proper when they are designed to affect a witness' credibility, test his memory or exhibit bias. *Shupe* v. *State,* 238 Md. 307, 311, 208 A.2d 590 (1965); *Kantor* v. *Ash,* 215 Md. 285, 290, 137 A.2d 661 (1958); *Ager* v. *Baltimore Transit Co.,* 213 Md. 414, 427-428, 132 A.2d 469 (1957). But it is recognized that the scope, range and extent of such interrogation rests in the sound discretion of the trial court. *Shields* v. *State,* 257 Md. 384, 392, 263 A. 2d 565 (1970); *Ridgeway, Inc.* v. *Seidman,* 243 Md. 358, 364, 221 A.2d 393 (1966); *Mezzanotte Const. Co.* v. *Gibons,* 219 Md. 178, 181, 148 A.2d 399 (1959). Here, it was unnecessary for Dr. Thomas to be further questioned in order to demonstrate his prejudice in favor of appellee. The jury was already cognizant of a possible bias since it had been shown that the two physicians were colleagues who had collaborated in the treatment of Mrs. Kruszewski."

Similarly, in the subject case, the witness had acknowledged participation in bribery attempts against public officials

and had admitted attempts to thwart justice by bearing false witness. Specifics of the offenses would neither have further blemished his escutcheon a whit, nor would the disclosure of the names of his associates have shown that he was either a lesser or a greater scoundrel. A contrary ruling, on the other hand, would have served to permit the witness stand to become the "slaughter house of reputations" of others. *See: Wigmore, supra,* p. 841.

We find neither abuse of discretion nor constitutional denial of confrontation in the ruling of the court.

(b) *The Witness Amick*

In the course of the direct examination of the witness John R. Amick, an Assistant Chief Examiner of the Federal Hone Loan Bank Board, the State attempted to have the Bank Board's examination records of Montgomery produced for introduction into evidence. The witness explained that he was forbidden to disclose examination reports in the absence of authority to do so. The State thereupon desisted from its effort to obtain the documents and limited its subsequent examination to an inquiry—without objection— to strictly hypothetical situations. This inquiry sought to determine what the witness as an examiner would do if he discovered that association funds had been placed in inactive, non-interest bearing checking accounts. The witness responded that: "We would confer with management and ask him why those accounts were not in something other than a non-interest bearing checking account, or at least bring his attention to it."

Defense counsel on cross-examination also sought unsuccessfully to obtain the examination reports and to elicit from the witness testimony as to their contents. Defense counsel requested the court to order the witness to produce the documents. The trial judge refused saying:

> "Now let me remind counsel that this case has been set for sometime, and Mr. Burgess and Mr. Mann have been attorneys for this defendant for many months, and they have the same right of subpoena, and interrogation, deposition, interrogatories. As a matter of fact more rights than the State has."



The trial judge also said:

> "And this member of the court has not, I am not familiar with any other member of the court that has been even asked to consider this question before this morning."

After further colloquy between court and counsel, the following inquiry was directed to the witness:

> "THE COURT: Mr. Amick, in this briefcase that is on the front table with a lock as I notice it, what is in that briefcase that is not available to the defense?
>
> THE WITNESS: All of the records wouldn't be available to the defense.
>
> THE COURT: All of them would be available?
>
> THE WITNESS: All wouldn't be.
>
> THE COURT: All would not be?
>
> THE WITNESS: That's right.
>
> THE COURT: Nothing in that suitcase would be available to them?
>
> THE WITNESS: That's right.
>
> THE COURT: Has this information been available to the State that is in that suitcase?
>
> THE WITNESS: No. All that information wasn't made available to the State.
>
> THE COURT: Well, are there some things in there that were made available to the State that you say are not available to the defense?

THE WITNESS: The monthly reports were made available to the State, and the—the State looked at the Management Questionnaires.

THE COURT: The Management Questionnaires are in evidence. So there is no problem with those.

MR. BURGESS: Just two of them are.

MR. LONGEST: Let me make the record clear. Those are the only two that have been made available to the State. So let's don't leave the inference that we have something that we are hiding."

In sum, the examination reports had been barred to both State and defense.

12 C.F.R. § 505.6 in pertinent part reads as follows:

"(a) *General rule.* Except as otherwise provided in this part or as may be specifically authorized by the Board,[3] information of the Board that has not been published in accordance with §505.3 and is not available to the public through other sources will not be made available to the public or otherwise disclosed if such information:

* * * * * * * * *

(2) Is contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of, the Board or a Federal Home Loan Bank, relating to the affairs of any member institution or affiliate thereof, or any other person engaged, or proposing to engage, in the savings and loan business; * * *"

Section 505.4 in pertinent part provides:

"It is the policy of the Board to disclose its records to the public, even though such records may, in the Board's discretion, be exempted from disclosure by



Section 552 of Title 5 of the United States Code or by § 505.6, wherever such disclosure can be made without resulting injury to a public or private interest intended to be protected by the foregoing statute * * *."

Section 505.7 may be summarized as authorizing issuance of subpoenas for the production of classified documents or information and for notification to the attorney for the party at whose instance the subpoena has been issued of the substance of the disclosure rules. Section 505.8 provides in substance that one aggrieved by denial of information or records may make written application to the general counsel of the Federal Home Loan Bank Board for their release. If refusal results from that application, a further appeal to the Board is provided by the section.

No effort had been made by appellant to utilize the provisions of law by which cou[illegible]use of confidential documents may be achieved. In the absence of proof of reasonable efforts to obtain the questioned documents for use as evidence, we will not assume that they would have been withheld upon application. We perceive no error in the rejection of appellant's belated effort to obtain them.

*4. Sufficiency of the Evidence*

The witness Kline thus described his use of non-interest bearing checking accounts of others as compensating balances for bank loans to himself or his corporations:

"Q. What is meant to you by compensating balances?

A. This is the balance that the banks require you to leave on deposit out of the proceeds of a loan. Usually it is the proceeds of a loan, so that they make a higher yield and it also helps in the growth of the bank because it increases deposits.

Q. Mr. Kline, let me give you the example of a loan of $100,000.00. Would you please apply the theory of

compensating a twenty percent compensating balance to that figure?

A. Yes. I would borrow a hundred thousand dollars. I would pay interest on a hundred thousand dollars. The bank wanted me to have the use of $80,000.00 and keep $20,000.00 on deposit, interest free, in a checkbook account. This money couldn't be used. It gave the bank a higher yield, and by making a hundred thousand dollar loan it also gave them an additional deposit of $20,000.00.

It was also a good practice for the bank to have this compensating balance because they have a right of offset if the loan was to the same entity that had the compensating balance and there was a default in the loan they could attach the money that was in the account.

Q. What, if anything, did you do about that practice of requiring the borrower to leave his own money in the checking account?

A. Well, some time in the middle sixties I came up with a method to lower my cost of borrowing and to give me the use of one hundred percent of the money borrowed.

Q. What was the method that you came up with?

A. The method of this was to have other entities or savings and loan associations supply compensating balances for my use.

Q. Now, how did you accomplish that, Mr. Kline?

A. Well, there were several ways.

One way took no money at all, and that was the easiest way, it was done with a savings and loan by me opening up a savings account at a savings and loan, getting interest on the savings account, taking the passbook or the savings certificate from the savings and loan to another institution to get my money back, and the interest I was receiving from the savings and loan would offset my interest borrowing costs at a bank, and in turn



I would get the savings and loan association where I deposited said amount of money to put it in an account I directed in a demand checking account, and I would have the bank know that I brought the account in so that I would get credit for it. So, in effect, I had use of one hundred percent of the money I borrowed, and I lowered my interest borrowing cost by twenty percent, actually twenty-five percent because if you only get the use of eighty percent of the money it is costing you an additional twenty-five percent because twenty percent is twenty-five percent of eighty.

Q. One-quarter?

A. Yes.

I cut my borrowing costs by twenty-five percent, and we were borrowing many millions of dollars, so it was a substantial savings."

Kline explained the role of appellant in the establishment of a compensating balance for his benefit by the deposit of funds of Montgomery Federal Savings and Loan Association in a non-interest bearing account in the Citizens Bank and Trust Company of Maryland:

"Q. Had you ever talked with Mr. Stathes about that amount of money?

A. Yes, sir.

Q. And an account at Citizens Bank and Trust Company?

A. Yes, sir.

The amount that I had talked to Mr. Stathes about was $50,000.00.

Q. What, if anything, did you say to Mr. Stathes concerning the $50,000.00 account at Citizens Bank and Trust Company?

A. This was in conjunction with me opening an account at Montgomery Federal for the same amount and having Montgomery Federal open an account at Citi-

zens Bank and Trust Company, and that the Association should not borrow any money from Citizens Bank and Trust because we both couldn't get credit for the same amount and if Montgomery Federal moved from the bank then Joel Kline couldn't get credit for it. That was the reason.

I was told by Mr. Stathes that they did their primary banking at Suburban Trust Company and that that was where they would borrow money if they needed it, the Association, so there would be no problem in them putting $50,000.00 at Citizens Bank and Trust at Riverdale, and they would not have to borrow any money.

Q. What purpose did you give Mr. Stathes for him placing money at the Citizens Bank and Trust Company?

A. So I would get credit for the money so I could use it as compensating balances.

Q. Did you use the phrase, 'compensating balances' with him?

A. I am not sure if I used that phrase. I would get credit for the money, so I would be borrowing against the moneys and not you. I may not have used the phrase 'compensating balances.'

* * * * * * * * *

Q. Mr. Kline, explain to the ladies and gentlemen of the jury, here, if you would, please, the connection between deposits and compensating balances insofar as Montgomery Federal was concerned.

A. These would be accounts that I would arrange to have put into Montgomery Federal for which I would be paid interest. In return Montgomery Federal would open a checking account at a bank which I directed the account be in, and the money would stay practically dormant at an agreed upon figure, which would be the same amount I kept on deposit at Montgomery Federal Savings and Loan."



Kline also testified that in return for the creation of compensating balance non-interest bearing accounts by Montgomery Federal Savings and Loan Association, he provided or arranged for multiple favors for appellant including the following:

1. free trips to Florida, Bimini and Las Vegas;
2. a "finder's fee" of $7500 for a loan to M & K Investments;
3. the purchase by Kline from Stathes of 5000 shares of stock in the Old Line National Bank at a price substantially higher than the price then quoted for the stock.

There was substantial corroboration that appellant participated in the creation of compensating balances for the use and benefit of Kline to the financial detriment of Montgomery. There also was substantial corroboration that he received favors in the form of cash and other valuable considerations. The trier of fact would be permitted to draw the reasonable inference that the two were interrelated. The appellant himself acknowledged that a non-interest bearing checking account was opened at Citizens Bank and Trust Company of Maryland because Joel Kline asked him to put it there. He acknowledged also that he had been provided free trips to Florida, Bimini and Las Vegas; that he had received the "finder's fee" to which Kline had referred; and that 5000 shares of his stock in Old Line National Bank had been sold to Kline at $15 per share. It is true, of course, that appellant vigorously maintained that the non-interest bearing checking account of Montgomery's funds in the Citizens Bank was opened to advance his corporation's interests and was related in no way to the receipt by him of favors. The jury was not obliged to accept that explanation. *Bromwell* v. *State,* 8 Md.App. 382, 387, 259 A.2d 577, 579-80 (1969).

Kline had testified that he or his secretary would be called from time to time by Citizens Bank officials advising that the association checking account had fallen below the required $50,000 balance. He added that he or she then would so inform an officer of Montgomery. The witness Soyers, Comptroller and Assistant Secretary of Montgomery, confirmed receipt of such calls from Kline or Kline's secretary. Soyers testified that he then would advise appellant of the calls and would be told "to bring the account balance up at my convenience." Soyers added that on one or two occasions appellant later return "to remind me to bring them [bank balances] up to $50,000." Appellant's denial of that testimony by both Kline and Soyers did no more than present a question of credibility properly to be resolved by the jury.

The record shows by a rational permissible inference that the deposit of Montgomery funds in a non-interest bearing checking account at Citizens Bank was initiated by the appellant in violation of his fiduciary duty to Montgomery and against its interest in order to achieve a personal gain detrimental to it.

The evidence was legally sufficient to convict. *Carter* v. *State*, 15 Md.App. 242, 247, 289 A.2d 837, 840 (1972).

*Judgment affirmed. Appellant to pay the costs.*



## APPENDIX B

IN THE COURT OF APPEALS OF MARYLAND

Petition Docket No. 2

September Term, 1976

(No. 237, September, 1975
Court of Special Appeals)

PETER T. STATHES

v.

STATE OF MARYLAND

### Order

Upon consideration of the petition for a writ of certiorari to the Court of Special Appeals in the above entitled case, it is

ORDERED, by the Court of Appeals of Maryland, that the said petition be, and it is hereby, denied as there has been no showing that review by certiorari is desirable and in the public interest. Judge Levine did not participate in the consideration of this petition.

/s/ ROBERT C. MURPHY
Robert C. Murphy
*Chief Judge*

[SEAL]

Date: May 5, 1976.

## APPENDIX C

IN THE CIRCUIT COURT FOR MONTGOMERY COUNTY

Criminal No. 14956

STATE OF MARYLAND

v.

PETER T. STATHES, *Defendant.*

**Notice of Appeal to the Supreme Court of the United States**

Notice is hereby given that Peter T. Stathes hereby appeals to the Supreme Court of the United States from the decision of the Court of Special Appeals of Maryland entered in this action on December 30, 1975, which was affirmed by the Court of Appeals of Maryland, the highest Court of the State, by its Order denying defendant's timely Petition For Certiorari entered in this action on May 5, 1976.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

WILLIAM H. BRAIN
10506 Connecticut Avenue
Kensington, Maryland 20795
(949-2617)

*Attorney for the Defendant*

July 26, 1976



## APPENDIX D

**Liquidity Regulations**

12 CFR—Chapter V, Federal Home Loan Bank Board

LIQUIDITY

SOURCE: §§ 523.10 through 523.14 appear at 34 F.R. 20413, Dec. 31, 1969, unless otherwise noted.

§ 523.10 Definitions.

For the purposes of this section, §§ 523.11 and 523.12:

(a) The term "cash" means cash on hand and unpledged demand deposits in a Federal Home Loan Bank, an insured bank, or the Bank for Savings and Loan Associations, Chicago, Illinois. The term "cash" does not include gold in any form.

(b) The term "insured bank" means a commercial bank whose deposits are insured by the Federal Deposit Insurance Corporation and which is not under the control or in the possession of any supervisory authority.

(c) The term "liquidity base" means—

(1) Prior to November 1, 1970, the amount of the member's net withdrawable accounts, or in the case of a member insurance company its policy reserve required by State law; and

(2) Beginning on November 1, 1970, the amount of the member's net withdrawable accounts or in the case of a member insurance company its policy reserve required by State law, plus the member's short-term borrowings.

(d) The term "net withdrawable accounts" means the amount of all withdrawable accounts less the unpaid balance of all loans on the security of such accounts.

(e) The term "short-term borrowings" means the amount of all borrowings which are payable on demand or which are due for payment in 1 year or less.

(f) The term "obligations of the United States" means evidences of indebtedness issued by the United States, or issued by any agency or instrumentality of the United States and fully guaranteed as to principal and interest by the United States.

(g) The term "liquid assets" means the total of cash, accrued interest on unpledged assets which qualify as liquid assets under this paragraph, or would so qualify except for their maturities, and the book value of the following unpledged assets (including such assets held subject to a repurchase agreement), as long as principal and interest on such assets are not in default:

(1) Time deposits in a Federal Home Loan Bank or the Bank for Savings and Loan Associations, Chicago, Ill.;

(2) Except (i) as the Board may otherwise direct in a specific case or (ii) pursuant to the provisions of paragraph (i) of this section, obligations of the United States having a remaining period to maturity of not more than 5 years:

(3) Obligations issued, or fully guaranteed as to principal and interest, by the following agencies or instrumentalities of the United States and having a remaining period to maturity of not more than 5 years:

(i) A Federal Home Loan Bank or Banks,

(ii) The Federal National Mortgage Association,

(iii) The Government National Mortgage Association,

(iv) A Bank or Banks for Cooperatives, including the Central Bank for Cooperatives,

(v) A Federal Land Bank or Banks,

(vi) A Federal Intermediate Credit Bank or Banks,

(vii) The Tennessee Valley Authority,



(viii) The Export-Import Bank of the United States,

(ix) The Commodity Credit Corporation, or

(x) The Federal Financing Bank.

(4) Time deposits in an insured bank including such time deposits held subject to a repurchase agreement and loans of unsecured day(s) funds (Federal funds or similar unsecured loans to insured banks) to an insured bank, if:

(i) The total of all time deposits, including loans of unsecured day(s) funds of the same member, in the same bank does not exceed the greater of (a) one-fourth of 1 percent of the total deposits of such bank (calculated on the basis of total deposits of such bank as shown by its last published statement of condition preceding the date each time deposit is made or acquired by a member), or (b) $40,000;

(ii) No consideration, other than discounting to a current market rate of interest, is received by the member from a third party in connection with the making or acquiring of such deposits (excluding loans of unsecured day(s) funds) by the member and no consideration is received by the member from a third party in connection with loans of unsecured day(s) funds by the member;

(iii) Except for loans of unsecured day(s) funds, such deposits are: (*a*) Negotiable and have remaining periods to maturity of not more than 1 year, (*b*) not negotiable and have remaining periods to maturity of not more than 90 days, or (*c*) not withdrawable without notice and the notice periods do not exceed 90 days;

(iv) The periods to maturity of loans of unsecured day(s) funds are not more than 6 months; and

(v) The claims of a lender of such unsecured day(s) funds are not subordinated in priority to claims of depositors in the insured bank to which such funds are loaned;

(5) Bankers' acceptances of an insured bank if:

(i) The total of all such acceptances of the same bank held by the same member does not exceed one-fourth of 1 percent of the total deposits of such bank (calculated on the basis of total deposits of such bank as shown by its last published statement of condition preceding the date each such acceptance is acquired by a member);

(ii) No consideration, other than discounting to a current market rate of interest, is received by the member from a third party in connection with the acquisition of such acceptances; and

(iii) The remaining periods to maturity of such acceptances are not more than 9 months; and

(6) general obligations (other than gold-related obligations) of any State, territory, or possession of the United States, or political subdivision of any of the foregoing, if:

(i) such obligations are and continue to be either (*a*) rated in one of the four highest grades as shown by the most recently published rating made of such obligations by a nationally recognized investment rating service or (*b*) issued by a public housing agency and have the full faith and credit of the United States pledged pursuant to section 1421a(c) or section 1437i(a) of Title 42 of the United States Code, as amended; and

(ii) the remaining periods to maturity of such obligations are not more than 2 years.

(h) The term "short-term liquid assets" means the total of cash, accrued interest on unpledged assets which qualify as liquid assets under paragraph (g) of this section, or would so qualify except for their maturities, and the book value of the following unpledged assets (including such assets held subject to a repurchase agreement):

(1) Time deposits specified in subparagraph (1) of paragraph (g) of this section;



(2) Obligations of the types specified in paragraphs (g)(2) and (g)(3) of this section either (i) having a remaining period to maturity of not more than 12 months or (ii) are qualified as short-term liquid assets under paragraph (i) of this section.

(3) Time deposits, including loans of Federal funds which qualify as liquid assets pursuant to the provisions of paragraph (g)(4) of this section and, except for such loans of Federal funds, are (i) negotiable and have remaining periods to maturity of not more than 6 months, (ii) not negotiable and have remaining periods to maturity of not more than 90 days or (iii) not withdrawable without notice and the notice periods do not exceed 90 days;

(4) Bankers' acceptances specified in paragraph (g)(5) of this section having a remaining period to maturity of not more than 6 months; and

(5) General obligations of the types specified in paragraph (g)(6)(i)(*b*) of this section having a remaining period to maturity of not more than 6 months.

(i) Before April 1, 1977, an investment which is continuously held by a member and which is counted as a liquid asset at the close of business on March 31, 1975, continues to count as a liquid asset notwithstanding and without regard to the maximum remaining period to maturity specified in paragraph (g) of this section. Before October 1, 1975, an investment which is continuously held by a member and which is counted as a short-term liquid asset at the close of business on March 31, 1975, continues to count as a short-term liquid asset notwithstanding and without regard to the maximum remaining period to maturity specified in paragraph (h) of this section.

[34 FR 20413, Dec. 13, 1969, as amended at 36 FR 3462, Feb. 25, 1971; 38 FR 30998, Nov. 9, 1973; 38 FR 32128, Nov. 21, 1973; 39 FR 9929, Mar. 15, 1974; 39 FR 17219, May 14, 1974; 40 FR 8324, Feb. 27, 1975; 40 FR 17245, Apr.

18, 1975; 40 FR 26672, June 25, 1975; 40 FR 41756, Sept. 9, 1975; 40 FR 59425, Dec. 24, 1975].

§ 523.11 Liquidity Requirements.

(a) *General.* For each calendar month, each member, other than a mutual savings bank as to which there is in effect the election provided for in paragraph (e) of this section, shall maintain an average daily balance of liquid assets in an amount not less than 6½ percent of the average daily balance of the member's liquidity base during the preceding calendar month, except as otherwise provided in paragraphs (b) and (d) of this section. For each calendar month, each member, other than a mutual savings bank or an insurance company, shall maintain an average daily balance of short-term liquid assets in an amount not less than 2½ percent of the average daily balance of the member's liquidity base during the preceding calendar month, except as otherwise provided in paragraphs (b) and (d) of this section.

(b) *Exception.* In lieu of using the average-daily-balance method prescribed in paragraph (a) of this section to compute its liquidity requirement, a member having less than $25 million in total assets as of the beginning of its current fiscal year may, by resolution of its board of directors, elect to maintain an average daily balance of liquid assets and short-term liquid assets in an amount not less than the applicable percentage (prescribed in paragraph (a) of this section) of its liquidity base as of the end of the preceding calendar month. Such election shall remain in effect unless sooner revoked by resolution of the member's board of directors, so long as the member continues to meet the above asset requirement.

(c) *Calculation of average daily balance.* For the purposes of this section, §§ 523.10 and 523.12, the "average daily balance of liquid assets," "average daily balance



of short-term liquid assets," and "average daily balance of the member's liquidity base," respectively, shall be calculated by adding the member's liquid assets, short-term liquid assets, or liquidity base, respectively, as of the close of each business day in a calendar month, and for any nonbusiness day, as of the close of the nearest preceding business day, and by dividing the respective total by the number of days in such month.

(d) *Reduction and suspension of liquidity requirements.* Whenever the Board deems it advisable in order to enable a member to meet withdrawals or to pay obligations, the Board may, to such extent and subject to such conditions as it may prescribe, permit the member to reduce its liquid assets below the minimum amount required by paragraph (a) of this section. Whenever the Board determines that conditions of national emergency or unusual economic stress exist, the Board may suspend any part or all of the liquidity requirements of paragraph (a) of this section for such period as the Board may prescribe. Any such suspension, unless sooner terminated by its terms or by the Board, shall terminate at the expiration of 90 days next after its commencement, but nothing in this sentence shall prevent the Board from again suspending any part or all of such liquidity requirements before, at, or after any such termination.

(e) *Election for mutual savings banks.* In lieu of the liquid-asset requirement imposed by the first sentence of paragraph (a) of this section, any member which is a mutual savings bank may, by resolution of its board of directors, elect to maintain liquid assets in accordance with the provisions of this paragraph. Any such member so electing shall maintain, for each calendar month, an average daily balance of liquid assets in an amount not less than 5 percent of the average daily balance of such member's liquidity base during the preceding calendar month, except as otherwise provided in paragraphs (b) and (d) of this

section, and such member shall maintain Federal funds and commercial paper in an aggregate amount not less than the difference between (1) the amount of liquid assets which, but for such election would have been required under the first sentence of paragraph (a) of this section and (2) the actual amount of liquid assets maintained by such member. Such election shall remain in effect, unless sooner revoked by resolution of such member's board of directors, so long as such member continues to meet the requirement specified in the preceeding sentence.

(Sec. 5A, 47 Stat. 727, as added by sec. 1, 64 Stat. 256, as amended; 12 U.S.C. 1425a) [34 F.R. 20413, Dec. 31, 1969, as amended at 36 FR 25150, Dec. 29, 1971; 40 FR 33029, Aug. 6, 1975]

§ 523.12 Deficiencies and Penalties.

(a) *Calculation of deficiency.* (1) Except as provided in subparagraph (2) of this paragraph, a member's liquid assets or short-term liquid assets for any calendar month are deficient in the amount that the average daily balance of such assets for such calendar month is less than the respective minimum amounts required pursuant to § 523.11.

(2) A member, other than an insurance company, may reduce any deficiency calculated pursuant to subparagraph (1) of this paragraph as follows:

(i) With respect to the first month of a current distribution period, by the amount of the member's aggregate net withdrawals (excess of withdrawals over cash savings received) from withdrawable accounts during the last 3 business days of the immediately preceding month and the first 10 calendar days of the current month; and

(ii) With respect to the second month of the same current distribution period, by one-half of such amount of aggregate net withdrawals; but



(iii) No such reduction of any deficiency shall operate to reduce the member's liquidity base as of the end of the immediately preceding distribution period.

(b) *Calculation of penalty.* The amount of penalty for any deficiency calculated pursuant to paragraph (a) of this section shall be determined by each member by multiplying the amount of such deficiency by one-twelfth of the sum of 2 percent and the annual interest rate for advances of 1 year or less charged by the member's Bank on the last day of the month in which such deficiency occurred. If there is a deficiency in the same calendar month in both liquid assets and short-term liquid assets, the penalty shall be calculated only on the larger deficiency. No penalty shall be calculated on any deficiency of $5,000 or less unless the Board shall otherwise direct in a specific case.

(c) *Assessment of penalty; compromise, remission, or mitigation.* The Board hereby assesses a penalty against each member in the amount calculated pursuant to paragraph (b) of this section. For good cause shown, the Board may, upon application by a member submitted through the Bank of which it is a member, compromise, remit, or mitigate, in whole or in part, any penalty herein assessed before collection thereof. The president of such Bank, or any other officer of such Bank designated by him, may, upon application and subject to such conditions as he may impose, so compromise, remit or mitigate such penalty, if he determines that:

(1) The penalty would have a seriously adverse effect upon the member; or

(2) The deficiency in liquid assets or short-term liquid assets resulted from either:

(i) The temporary disruption of normal operations because of negotiation or implementation of a merger or similar transaction; or

(ii) Any situation beyond the control of the institution's management, including but not limited to:

(*a*) A breakdown or unforeseen delay in mail or other form of communication;

(*b*) An unexpectedly heavy withdrawal of savings coupled with large disbursements on commitments;

(*c*) A natural disaster; or

(*d*) Abnormally heavy withdrawals caused by harmful rumors.

However, no such penalty may be compromised, remitted, or mitigated if the member has failed to observe any condition imposed in connection with a prior compromise, remission, or mitigation of any such penalty.

(Sec. 5A, 47 Stat. 727, as added by 64 Stat. 256, as amended by sec. 4, 82 Stat. 856; 12 U.S.C. 1425a) [23 F.R. 9886 Dec. 23, 1958, as amended at 35 F.R. 11462, July 17, 1970]

§ 523.13 Reports; Records.

(a) *Reports.* If there is a deficiency pursuant to the provisions of paragraph (a) of § 523.12 and a penalty is assessed pursuant to the provisions of paragraph (c) of § 523.12, the member shall submit to the Bank of which it is a member, not later than the 10th calendar day of the month for which the penalty is assessed, a report with respect to such penalty and related matters in form prescribed by the Board. Copies of this form may be obtained from the Federal Home Loan Bank Board, Washington, D.C., or from any Bank.

(b) *Records.* Each member shall maintain such records as may be required to verify such member's compliance with the liquidity requirements prescribed by the Board. Such records shall be made available to the Board, or its representatives, during the course of each supervisory examination and at such other times as the Board may direct.



(12 U.S.C. 1425a)

§ 523.14 Payment of Penalty

At the time each report is submitted pursuant to the requirements of paragraph (a) of § 523.13, the member shall enclose with such report a check, payable to the Bank of which it is a member, in the amount of the penalty assessed for the month covered in such report, unless the member makes the application referred to in paragraph (c) of § 523.12.

(12 U.S.C. 1425a)

Supreme Court, U. S.
FILED
AUG 26 1976
MICHAEL RODAK, JR., CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1976

## No. 76-149

PETER T. STATHES,

*Appellant,*

v.

STATE OF MARYLAND,

*Appellee.*

ON APPEAL FROM THE COURT OF SPECIAL APPEALS OF MARYLAND

## MOTION TO DISMISS

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IN THE

# Supreme Court of the United States

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OCTOBER TERM, 1976

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## No. 76-149

---

PETER T. STATHES,

*Appellant,*

v.

STATE OF MARYLAND,

*Appellee.*

---

ON APPEAL FROM THE COURT OF SPECIAL APPEALS OF MARYLAND

---

## MOTION TO DISMISS APPEAL

Appellee moves to dismiss the appeal from the judgment and opinion of The Court of Special Appeals of Maryland entered on December 30, 1975. That judgment affirmed the Appellant's conviction for embezzlement in the Circuit Court for Montgomery County, Maryland on December 10, 1974. The grounds for this motion to dismiss appeal are that Appellant has not raised any substantial federal question in this appeal.

## OPINION

The opinion below is reported at 29 Md. App. 474, 349 A.2d 254 (1975).

## JURISDICTION

The Appellant is asserting jurisdiction in this court by virtue of the provisions of Title 28 U.S.C., § 1257(2) in that it is alleged that the judgment of the highest court of the State of Maryland upholding the validity of a state statute, as applied, is alleged to be repugnant to the banking laws of the United States and criminal sanctions thereto.

## QUESTION PRESENTED

Is the prosectution by the State of Maryland of the president of a federally chartered savings and loan association preempted by federal law where the facts show that the Defendant used his association's funds as compensating balances?

## STATEMENT OF FACTS

The Appellant, Peter T. Stathes, was shown by overwhelming evidence to have set up static checking accounts in the Bank of Bethesda and Citizens Bank and Trust Company of Maryland using Montgomery Federal Savings and Loan Association funds. The testimony at his trial indicated that such accounts were unusual and were not categorized as daily operating accounts. Further testimony indicated that the Citizens Bank and Trust Company considered a $50,000.00 deposit made by Stathes in the name of Montgomery Federal to be a compensating balance for a loan extended to Joel Kline. Additional evidence disclosed that such accounts were brought to balance when Joel Kline's office was notified that the accounts were below



the compensating balance minimum. The testimony of William Brain indicated that as a member of the Board of Directors had he known that such funds were being used as compensating balances he would have disallowed the practice. Although accounts were opened on authority of the Board of Directors, Brain had no reason to suspect that either of the two accounts were for compensating balances since the Appellant never discussed it. The witness also did not know the extent, if any, of the Appellant's business connections with Joel Kline.

On December 10, 1974 a Jury sitting in the Circuit Court for Montgomery County, Maryland, found the Appellant guilty of Count I of Criminal Number 14956 charging embezzlement in violation of Article 27 § 132 of the Annotated Code of Maryland.

The Appellant subsequently appealed his convictions to the Court of Special Appeals of Maryland which tribunal in a reported opinion upheld the jurisdiction of the State of Maryland to try Appellant for his offenses. The Court of Appeals of Maryland declined to issue a writ of certiorari to the Court of Special Appeals in that case and so denied the Appellant any further relief.

## STATUTES INVOLVED

**Title 12, U.S.C., § 1425a:**

> "No member of a Federal Home Loan Bank shall make or purchase any loan at any time when its cash and obligations of the United States are not equal to such amount as the Federal Home Loan Bank Board shall by regulations prescribe: *Provided*, That such amount shall not be less than 4 per centum or more than 8 per centum of the obligation of the member on withdrawable accounts or, in the case of any member insurance company, such other base as the Board may

determine to be comparable. The Board is authorized in said regulations to prescribe from time to time different amounts, within the limitations hereinbefore specified, for different classes of member institutions, and for such purposes the Board is authorized to classify such members according to type of institution, size, location, rate of withdrawals, or such other basis or bases of differentiation as the Board may deem to be reasonably necessary or appropriate for effectuating the purposes hereof. Failure to comply with the provisions hereof shall constitute ground for removal from membership."

**Title 18, U.S.C., § 657:**

"Whoever, being an officer, agent or employee of or connected in any capacity with the Reconstruction Finance Corporation, Federal Deposit Insurance Corporation, Home Owners' Loan Corporation, Farm Credit Administration, Federal Housing Administration, Federal Crop Insurance Corporation, Farmers' Home Corporation, the Secretary of Agriculture acting through the Farmers' Home Administration, or any land bank, intermediate credit bank, bank for cooperatives or any lending, mortgage, insurance, credit or savings and loan corporation or association authorized or acting under the laws of the United States or any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or any small business investment company, and whoever, being a receiver of any such institution, or agent or employee of the receiver, embezzles, abstracts, purloins or willfully misapplies any moneys, funds, credits, securities or other things of value belonging to such institution, or pledged or otherwise intrusted to its care, shall be fined not more than $5,000 or imprisoned not more than five years, or both; but if the amount or value embezzled, abstracted, purloined or misapplied does not exceed $100, he shall be fined not more than $1,000 or imprisoned not more than one year, or both."



**Title 18, U.S.C., § 3231:**

"The district courts of the United States shall have original jurisdiction, exclusive of the courts of the States, of all offenses against the laws of the United States.

Nothing in this title shall be held to take away or impair the jurisdiction of the courts of the several States under the laws thereof."

## Liquidity Regulations

12 CFR — Chapter V, Federal Home Loan Bank Board

LIQUIDITY

### § 523.10 Definitions.

For the purposes of this section, §§ 523.11 and 523.12:

(a) The term "cash" means cash on hand and unpledged demand deposits in a Federal Home Loan Bank, an insured bank, or the Bank for Savings and Loan Associations, Chicago, Illinois. The term "cash" does not include gold in any form.

. . .

(g) The term "liquid assets" means the total of cash, accrued interest on unpledged assets which qualify as liquid assets under this paragraph, or would so qualify except for their maturities, and the book value of the following unpledged assets (including such assets held subject to a repurchase agreement), as long as principal and interest on such assets are not in default:

. . .

(G)(4)(ii) No consideration, other than discounting to a current market rate of interest, is received by the member from a third party in connection with the making or acquiring of such deposits (excluding loans of unsecured day(s) funds) by the member and no consideration is received by the member from a third party in connection with loans of unsecured day(s) funds by the member;

**§ 523.11 Liquidity Requirements.**

(a) *General.* For each calendar month, each member, other than a mutual savings bank as to which there is in effect the election provided for in paragraph (e) of this section, shall maintain an average daily balance of liquid assets in an amount not less than 6½ percent of the average daily balance of the member's liquidity base during the preceding calendar month, except as otherwise provided in paragraphs (b) and (d) of this section. For each calendar month, each member, other than a mutual savings bank or an insurance company, shall maintain an average daily balance of short-term liquid assets in an amount not less than 2½ percent of the average daily balance of the member's liquidity base during the preceding calendar month, except as otherwise provided in paragraphs (b) and (d) of this section.

. . .

(c) *Calculation of average daily balance.* For the purposes of this section, §§ 523.10 and 523.12, the "average daily balance of liquid assets," "average daily balance of short-term liquid assets," and "average daily balance of the member's liquidity base," respectively, shall be calculated by adding the member's liquid assets, short-term liquid assets, or liquidity base, respectively, as of the close of each business day in a calendar month, and for any nonbusiness day, as of the close of the nearest preceding business day, and by dividing the respective total by the number of days in such month.

**Art. 23, § 161B, Anno. Code Md. (1966 Rep. Vol.)**

(a) *Definition of "association".* — As used in this subtitle, the word "association" shall mean building, savings and loan or homestead association or any other similar association by whatever name called.



(b) *Domestic and foreign associations.* — The provisions of this article shall apply to all associations heretofore or hereafter organized under the laws of this State; and to all foreign associations duly authorized to do business in this State;

(c) *Federal associations.* — Unless federal laws or regulations provide otherwise, federal associations incorporated pursuant to the Homeowners Loan Act of 1933, as amended, and their members shall be subject to the provisions of this subtitle and shall possess all of the rights, powers, privileges, immunities and exemptions granted by this article to associations operating hereunder and to the members thereof. (1961, ch. 205.)

**Art. 23, § 159 (1969 Cum. Sup.)**

Any association eligible to become a member of the federal home loan bank system, may convert itself into a federal savings and loan association, as provided for in the act of the Congress of the United States, approved the 13th day of June, 1933, entitled "The Home Owners Loan Act of 1933," with amendments, with the same force and effect as though originally incorporated under such act of Congress, and the procedure to effect such conversion shall be as follows:

. . .

(d) *Effect of taxation or doing business.* — For purposes of taxation or doing business within this State, any association availing itself of the privileges of this section shall be regarded as a domestic corporation of this State, and its property, shares and assets shall be taxed in the same manner and to the same extent as the property, shares and assets of domestic associations of this State, and shall in every other respect be regarded as a domestic corporation of this State.

**Article 27, § 132, Annotated Code of Maryland:**

"If any executor, administrator, guardian, committee, trustee, receiver or any other fiduciary shall

fraudulently and willfully appropriate to any use and purpose not in the due and lawful execution of his trust, any money or any other thing of value which may come into his hands as such executor, administrator, guardian, committee, trustee, receiver, or in any other fiduciary capacity, or secrete it with a fraudulent intent to appropriate it to such use or puspose, he shall be deemed guilty of embezzlement, and shall be punished upon conviction by imprisonment in the penitentiary for not less than one year nor more than five years."

**Estates and Trusts Article, § 15-201(c):**

"(a) *General.* — In this subtitle the following words have the meanings indicated.

. . .

"(c) *Fiduciary.* — 'Fiduciary' includes a trustee under any trust expressed, implied, resulting or constructive, executor, administrator, guardian, conservator, curator, receiver, trustee in bankruptcy, assignee for the benefit of creditors, partner, agent, officer of a corporation, public or private, public officer, or any other person acting in a fiduciary capacity for any person, trust, or estate."

## ARGUMENT

**THE PROSECUTION BY THE STATE OF MARYLAND OF THE PRESIDENT OF A FEDERALLY CHARTERED SAVINGS AND LOAN ASSOCIATION IS NOT PREEMPTED BY FEDERAL LAW WHERE THE FACTS SHOW THAT THE DEFENDANT USED HIS ASSOCIATION'S FUNDS AS COMPENSATING BALANCES.**

The thrust of the Appellant's argument establishing an alleged substantial federal question is that pursuant to federal statutory and regulatory scheme Congress has preempted any State prosecution of the officers of federally chartered savings and loan associations for State offenses committed during the conduct of their office. Specifically he suggests that Congress when it enacted Title 18, U.S.C., §657 prohibiting willful misapplication of funds by an officer or employer of a federal savings and loan association, preempted Maryland's fraudulent misappropriation by a fiduciary State statute. Thus the Appellant seems to be suggesting that the offense in the instant case is covered by federal criminal sanctions.



On the other hand the Appellant's argument under *Easton v. Iowa,* 188 U.S. 220, 23 S. Ct. 288, 47 L. Ed. 452 (1903) together with the citing of the provisions of Chapter 5 of 12 CRF, Federal Home Loan Bank Board Regulations, seems to indicate that the Appellant feels that he is operating *pursuant* to federal law and has not committed a federal crime.

### A. Federal Criminal Sanctions

It is submitted that the Appellant's reliance in the first instance on the case of *Easton v. Iowa, supra,* to suggest preemption is misplaced. It is submitted that the thrust of the decision in *Easton* was that the Appellant there received deposits knowing his institution to be insolvent contrary to Iowa criminal code provisions; Easton's actions were found to be permissible under federal regulations. It was held that although states have the power to define and punish crimes by general law applicable to all persons within its jurisdiction they are without power to make special laws applicable to banks organized and operating under the laws of the United States. It was felt that the operations of national banks should not be subjected to limitations and restrictions imposed by State legislation which are contrary to federal statutes organizing the national banks. Perhaps the most telling factor, however, in the *Easton* case is that the Supreme Court found that the Supreme Court of Iowa misinterpreted federal law when it stated that there was no act of Congress prohibiting the receipt of deposits by national

banks or their officers when the bank is insolvent. Mr. Justice Shiras speaking for the Supreme Court listed the regulations and procedures by which a federal bank might nonetheless receive deposits notwithstanding the fact that it might be insolvent. In essence the Supreme Court found that federal banking regulations would permit the comptroller of the treasury to continue operating a bank and to continue receiving deposits under such circumstances. Accordingly it is submitted that the basic proposition in the *Easton* decision is that the Iowa statute made unlawful that which could be lawful under federal law.

Furthermore the Appellant asserts that the provisions of 12 CFR, §§ 523.10 through 523.14 control the disposition of liquidity accounts and that the Appellant's activities with regard to the deposits were proper thereunder. Therefore, Maryland has been preempted under the *Easton* decision. First of all nothing in the Federal Home Loan Bank Board regulations requires or suggests that compensating balances may be used to maintain liquidity requirements thereunder. Secondly, liquid assets are defined as being among other things, cash and accrued interest on unpledged assets; § 523.10(a) defines the term "cash" as unpledged demand deposits. Clearly under the circumstances in the instant case an account used as a compensating balance, where a minimum deposit is constantly maintained, is not an unpledged demand deposit within the meaning of the term cash as it relates to liquidity requirements.

In 1969 the General Counsel of the Federal Home Land Bank Board had occasion to comment in an opinion with regard to whether or not a federal savings and loan association has authority to engage in the granting of compensating balances. He found that



while it was true that a federal savings and loan association might deposit funds in a bank or demand deposit accounts, such deposits must basically further the goals and objectives of the association. It was felt that any restriction upon the deposit or any right of any other party or parties in the deposit would mean that the deposits would not qualify as cash in satisfaction of the liquidity requirements. It would seem then that the right of withdrawal as demonstrated by the evidence in the instant case was not to be solely determined by the depositor, *i.e.,* Montgomery Federal Savings and Loan Association, but rather was to be determined by the two banks who held the accounts as compensating balances. The testimony clearly indicates that whenever the compensating balances account got below a certain minimum deposit the banks involved notified Joel Kline who in turn had Montgomery Federal Savings and Loan Association return the balances of the accounts to the accepted minimum. Clearly the depositors of Montgomery Federal Savings and Loan Association did not have unimpaired rights to the funds and accordingly they should not have qualified as liquid assets or unpledged cash. It is interesting to note that William Brain testified at the trial on the merits that had he as a member of the Board of Directors known that the Appellant, Stathes, was using the funds in the manner so disclosed, he would have disallowed the practice (T. E. 130-131).

See Appendix A for the May 28th, 1969 opinion of Arthur W. Leibold, Jr., general counsel, Federal Home Loan Bank Board. Similarly the United States Court of Appeals for the Tenth Circuit in *U.S. v. Brookshire*, 514 F.2d 768 (1975) concluded that in a prosecution for misapplication of bank funds the use of an inter-bank deposit as a compensating balance for a loan to the

president of the depositing bank was a willful misapplication in violation of Title 18, U.S.C., §656.[1] Thus it would seem without further question that the Appellant's activities as disclosed by the evidence below, and to which he can raise no objection here, clearly indicates that he violated state as well as federal law and regulations in making the compensating balances for Joel Kline.

B. Extent Of State Incursion.

It is necessary to comment upon two of the cases cited by the Appellant. In the case of *People of the State of New York v. Eno,* 155 U.S. 89, 15 S. Ct. 30, 39 L. Ed. 80 (1894), the Supreme Court reversed the Second Circuit Court of Appeals in *Eno, supra,* on the grounds that the Second Circuit should have permitted the highest court of the State of New York to first decide whether or not it had jurisdiction to try the petitioners. The court declined to consider the merits of the appeal whatsoever and directed that the judgment of the Second Circuit was reversed and directed that a petition for writ of habeas corpus be dismissed as being without jurisdiction. Secondly, in *Cross v. North Carolina,* 132 U.S. 131, 10 S. Ct. 47, 33 L. Ed. 287 (1889) the Supreme Court upheld the conviction of the Appellant, the president of the State National Bank of Raleigh, North Carolina, for forgery. The court felt that in that particular that since the crime that Cross was charged with was not one specifically against the United States but rather was a fraud against the people of the State of North Carolina then that State could successfully prosecute the Appellant. Mr. Justice Harlen speaking for the Supreme Court stated at 132 U.S. at pages 139 and 140:

[1] Similar to §657 except that it relates to Federal Banks rather than savings institutions.



"The argument on behalf of the plaintiffs in error fails to give effect to the established doctrine that the same act, or series of acts, may constitute an offense equally against the United States and the state, subjecting the guilty party to punishment under the laws of each government. [citations omitted] . . . If it were competent for Congress to give exclusive jurisdiction to the courts of the United States of the crime of falsely making or forging promissory notes, purporting to be executed by individuals, and made payable to or at a national bank, or the crime of uttering or publishing as to any such falsely made or forged notes, it has not done so. Its legislation does not assume to restrict the authority which the states have always exercised of punishing in their own tribunals the crime of forging promissory notes, and other commercial securities, executed by private persons, and used for purposes of private business. The forging of such instruments is nonetheless injurious to the welfare of the people of the state because they happened to be made payable to or at banking associations which come into existence under the authority of the United States. . . . The forgery may have been committed in order that the instrument forged might thereafter become the basis of false entries upon the books of the bank. But that circumstance cannot defeat the authority of the state, charged with the duty of protecting its own citizens, from punishing the forgery as in itself a distinct, separate offense, committed within its limits and against its laws."

In the case at bar the fraud perpetrated was not only against the federal banking system and against the United States, but is also against the depositors and shareholders of Montgomery Federal Savings and Loan Association, presumably some of which are Maryland citizens.[2]

[2] Not to mention the fact that the locus of the Association's assets and the deposits in question was in Maryland.

The prosecution of the Appellant in this case was not an attempt by the State of Maryland to override the policy of any federal statute, but rather it was an attempt to assert jurisdiction under a statute applicable to all fiduciaries in the State of Maryland. The statute in question does not have any relationship to an attempt to assert control of federally chartered associations. See *Uphaus v. Wyman,* 360 U.S. 72, 79 S. Ct. 1040, 3 L. Ed. 2d 1090 (1959). The Court of Special Appeals of Maryland found that different sovereignties had the right to prosecute in such circumstances, citing *Westfall v. U.S.,* 274 U.S. 256, 47 S. Ct. 629, 71 L. Ed. 1036 (1927) and others. It is submitted that the language quoted by the Court of Special Appeals of Maryland at 29 Md. App. page 481 is applicable:

> "An act denounced as a crime by both federal and state sovereignties is an offense against the peace and dignity of both, and may be punished by each. *U.S. v. Jackson,* 470 F.2d 384 (5th Cir. 1972)."

Title 12 U.S.C., § 1464(d) (4) (A) permits the removal of an association officer who breaches his fiduciary duty. Title 12, U.S.C., § 1730(g) (1) authorizes the removal of an officer of any association insured by the Federal Savings and Loan Association Corporation for breach of his fiduciary duty. Clearly, the Homeowners' Loan Act of 1933 assumed the existence of fiduciary duties from its inception. Similarly, Maryland statutes impose fiduciary duties upon officers of savings and loan associations. Federal savings and loan associations fell, at the time of the incident, within the scope of Article 23, § 161, et seq. Article 23, § 161B(c) (1966 Rep. Vol.) stated:

> "Unless federal laws or regulations provide otherwise, federal associations incorporated pursuant to the Homeowners' Loan Act of 1933, as amended, shall be subject to the provisions of this subtitle . . . ."



Furthermore, Article 23, § 159(d) (1969 Cum. Sup.) permitted State chartered savings and loan associations to convert to membership in the Federal Home Loan Bank System. That section further provided that any savings and loan association that did convert shall "for the purposes of taxation or doing business in this state . . . be regarded as a domestic corporation of this state . . . ." Significantly, Montgomery Federal Savings and Loan Association comes within this provision since it was originally a state chartered institution and later converted.

Clearly, since Montgomery Federal Savings and Loan Association is a domestic corporation of this state, it is subject to the provisions of the Maryland Uniform Fiduciaries Act, Estates and Trust Article, § 15 201 et seq. The definition of fiduciary applies to the officer of a corporation as well as any other person acting in a fiduciary capacity, for any person, trust or estate. Person is defined as including a corporation or partnership or other association. Obviously, the Appellant was an officer of a savings and loan association who owed the same fiduciary duties to the association and its members, depositors and stockholders as a corporate officer owes to his corporation and stockholders. Under such circumstances it is suggested that the State of Maryland has a legitimate interest in the deposits, obligations and other activities of Montgomery Federal Savings and Loan Association to the extent that the interests of its citizens exist in those deposits. Therefore utilizing the general proposition that a national bank is subject to state law unless that law interferes with the purposes of its creation or destroys its sufficiency or is in conflict with some

paramount federal law, it is submitted that Maryland can enforce its criminal breach of fiduciary duty statutes against the Appellant in the instant case, *Lewis v. Fidelity and Deposit Company,* 292 U.S. 559, 54 S. Ct. 848, 78 L. Ed. 1425 (1934). In *Lewis, supra,* Mr. Justice Brandeis speaking for the Supreme Court held that the obligations of a bank to a state may be defined by the law of that state. In the instant case it is submitted that the savings and loan association was mandated to be operated in such a way that its president and board of directors did not breach their fiduciary duties to their members. See also *Jennings v. United States Fidelity & Guaranty Company,* 294 U.S. 216, 55 S. Ct. 394, 79 L. Ed. 869 (1935).

In the case of *In Re Election of Directors,* 51 N.Y. Supp. 2d 816 (1944) the New York Supreme Court was called upon to decide a question involving a State savings and loan association which converted to a federal savings and loan association under the Home-owners' Loan Act. The New York court was called upon specifically to decide the question of whether or not the election for Board of Directors violated the charter of the savings and loan association. The court held that it had jurisdiction to consider the issue since national banks are citizens of the State in which they are located, and although subject to the paramount authority of the United States they are also subject to State laws as to their affairs unless such laws conflict with the paramount law of the United States. The court found that since the federal statutes in question contain no provisions for review of election of directors, it had jurisdiction. In the instant case there is no apparent conflict between the policy of the State of Maryland and the national banking policies. Therefore, Maryland should be permitted to enforce its criminal statute. *Uphaus v. Wyman, supra, Abbate v. United States,* 359



U.S. 187, 79 S. Ct. 666, 3 L. Ed. 2d 29 (1959); *People of California v. Zook,* 336 U.S. 725, 69 S. Ct. 841, 93 L. Ed. 1005 (1949); and *Cross v. North Carolina, supra.* See also *Erich v. Webb,* 336 F.wd n53 (9th Cir. 1964).

Pursuant to the provisions of Title 18, U.S.C., § 3231:

> "The district courts of the United States shall have original jurisdiction, exclusive of the courts of the State, of all offenses against the laws of the United States.
>
> Nothing in this Title shall be held to take away or impair the jurisdiction of the courts of the several states under the laws thereof."

Clearly Maryland is not attempting to divest the United States of original jurisdiction of offenses against the United States. In the instant case Maryland is not attempting to prosecute the Appellant for violation of federal law, but rather is attempting to prosecute the Appellant for violation of state law. As it has been stated before, the mere fact that an offense is committed against both sovereignties is not sufficient to conclude that federal law has preempted prosecution in the area.

## CONCLUSION

For the foregoing reasons, it is respectfully submitted that Appellant's appeal from the Court of Special Appeals of Maryland should be dismissed.

Respectfully submitted,

FRANCIS B. BURCH,
Attorney General
of Maryland,

CLARENCE W. SHARP,
Assistant Attorney General,
Chief, Criminal Division,

BERNARD A. RAUM,
Assistant Attorney General,
Counsel for Appellee.

# APPENDIX A

## FEDERAL HOME LOAN BANK BOARD

Inter-office Communication

From Office of the General Counsel Date 5-28-69

To: Paul F. Bowman, Jr.
Regional Supervisor
Office of Examinations
and Supervision

Subject, American FS&LA of
Duval County
Jacksonville, Florida

In your memorandum of April 11, 1969 you ask for the opinion of this office regarding the following situation:

> Since 1965 the subject association has been depositing funds in commercial banks for the benefit of finance companies. Specifically, the banks require, when granting a line of credit to finance companies, that the companies maintain, in the form of demand deposits, compensating balances amounting to 15.0 percent of the credit line. In lieu of maintaining their own balances the finance companies arrange for third parties (in this case, the association) to open such accounts. The bank pays the association nothing for these deposits; the finance companies pay the association one-half of 1.0 percent above the prime rate — currently a total of 7.0 percent.

It is the contention of the Supervisory Agent that a Federal savings and loan association has no authority to engage in transactions of this type. The management of the association maintains that since the deposits may be withdrawn at any time without notice to the finance companies, such deposits provide a method by which income can be earned by the funds which are available to satisfy the liquidity requirements of §§ 545.8-2 and 523.12 of the Regulations.

First, as to the nature of the transaction, it is apparent that although the maintenance of a compensating

balance is similar to making a loan, it is not in fact a loan so long as the unimpaired right to the funds remains in the association. The power of a Federal savings and loan association to deposit funds in a bank demand deposit account is not specifically stated in the Charter or regulations but is rather an implied power. The liquidity requirements of the Bank Regulations presume the right of an association to deposit funds in a Bank. An implied power is, however, a limited one; it must further the basic goals and objectives of the association.

There is some doubt as to whether, under present law and regulations, a Federal association can legitimately be compelled to lower its liquidity ratio and increase the number and amounts of its loans, whatever may be our opinion of a high liquidity ratio. At some point the maintenance of a very conservative attitude toward liquidity might result in a complete abandonment of the fundamental objective of a Federal association, *i.e.*, promoting home financing; however, the basis for penalizing an institution when this point is reached is unclear. As long as an association does not violate the provisions as to investments in § 545.9, and does not make loans contrary to the Federal regulations, there is no obvious basis for compelling a Federal association to make more loans on the security of first liens on real estate.

Secondly, above I stated that the association must at all times have an unimpaired right to the funds. By this I mean that the right of withdrawal is not limited by an agreement with either the finance company or the bank. If the bank has any right whatsoever to set off the deposit against the credit advances to the finance company, the entire transaction would be improper in that it would be a financial transaction unrecognized and unauthorized by the lending and investment regulations. Further, any restriction upon the deposit, or any right of other party or parties in the deposit would mean that said deposit would not qualify under §§ 545.8-2 and 523.12 of the Federal Home Loan Bank System Regulations as cash in satisfaction of the



liquidity requirement. Section 523.12 provides in subsection (b):

> (b) The term "cash" means cash on hand, unpledged deposits in a Federal Home Loan Bank or State bank performing similar reserve functions, and *unpledged demand deposits in domestic banks,* not under the control or in the possession of appropriate supervisory authority. [Emphasis supplied.]

By using the term "unpledged" it appears that the intention of the Board was that the funds so deposited should be completely unfettered, *i.e.,* no one except the depositing association should have any right, legal or equitable, in the funds. From this it follows that only the depositor and no one else should have the right to withdraw said funds.

In addition, your memorandum asked my opinion as to what effect the proposed liquidity regulations, contained in Board Resolution No. 22,594 issued February 18, 1969, would have on the situation discussed above. First, the requirement as to the asset being "unpledged" as contained in § 523.10(a) of the proposed regulation remains unchanged. If, as was mentioned above, anyone had any rights which prevented the association from having the complete and absolute right to withdraw the funds at any time such funds would not be considered as "unpledged". Secondly, it should be noted that the prohibition contained in § 523.10(a) (4) (ii), as proposed, that "no consideration is received by the member from a third party in connection with the making or acquiring of such deposit by the member", does not pertain to demand deposits. Since the proposal contained in said Board Resolution is still open for change and revision, the Office of Examinations and Supervision might wish to recommend the inclusion of a prohibition similar to the one contained in § 523.10(a) (4) (ii) in § 523.10(a) (1) if in the judgment of your Office the practice discussed in this opinion is detrimental to

the safe and sound management of members of the Federal Home Loan Bank System.

ARTHUR W. LEIBOLD, JR.,
General Counsel,
By: /s/ MAX WILFAND,
Deputy General Counsel.